§ 313.837 Report on Competitiveness

Introduction

Section 313.837, RSMo. requires the Commission to report annually to the General Assembly "the status of the competitiveness of Missouri excursion gambling boats when compared to the gaming tax rate of adjoining states and the effects of the loss limits imposed by subdivision (3) of Section 313.805, RSMo., on the competitiveness of the gaming industry in Missouri."

Competitive Impact of Missouri's Gaming Tax Rate

The gaming tax rates imposed on riverboat gaming operations in Missouri have not changed since the first licenses were issued in May 1994. Missouri law imposes an 18% tax on the adjusted gross receipts (AGR) of riverboat gaming operators.[1] In addition, a local tax of 2% on AGR is collected by the state and distributed to each home dock city or county.[2]

The statute also imposes an admission fee on the operators of excursion gambling boats in the amount of two dollars ($2) per patron, per excursion, which is split between the home dock community and the state.[3] Furthermore, pursuant to section 313.824, RSMo., excursion gambling boat operators are charged for the cost of gaming agents that are assigned to the riverboat with the responsibility of protecting the public. While the cost of Commission agents varies with each operation, the average annual cost is approximately $587,018 per gaming facility.

Effective Gaming Tax Rate

States that have legalized gaming have devised a variety of different taxes, fees and assessments that apply to casino operators. In addition, varying regulatory policies have a significant impact on the amount of revenue a casino generates. In order to compare the effects of such policy decisions, industry analysts and those who research public policy issues related to gaming have devised a simple formula to compare the public costs paid by gaming operators in various states. Commonly referred to as the "effective tax rate" the formula is simply the total of all gaming taxes, fees and assessments as a percentage of gross revenue.[4]

The effective tax rate is a helpful tool on at least two levels. First, it consolidates into one number all gaming taxes, fees and assessments that casino operators are required to pay. These expenses are typically separated in public report tables and it becomes difficult to evaluate the total costs being paid by a casino operator in order to maintain the privilege of being licensed. In addition, assessments against a licensee for various regulatory activities are often not reflected in the

[1] Adjusted gross receipts are defined by Section 313.800, RSMo., as "the gross receipts from licensed gambling games and devices less the winnings paid to wagerers." In other words, the amount the casino "wins" from patrons. It is often referred to as "casino win". The tax on AGR is set forth in Section 313.822, RSMo.

[2] Section 313.822, RSMo.

[3] Section 313.820, RSMo.

[4] The formula only includes taxes and fees that are unique to the gaming industry. Therefore, such things as state income or sales tax are not included.

revenue reports that are distributed by the states.[5] However, these costs can be significant and must be considered in evaluating the effect of taxes and regulations on the economic impact of gaming.

The effective tax rate is instructive in comparing the impact of varying state regulatory schemes on gaming revenues. When regulations limit the amount of revenue that a gaming facility can generate, it will be reflected in the effective tax rate. Naturally, there are some instances, such as the $500 loss limit in Missouri or the betting limits in Colorado or South Dakota, where the policy objective is intended to reduce revenue. In such cases, the effective tax rate is a useful tool in analyzing the cost of those policy objectives.

The effective tax rate is also a good indicator for evaluating many ramifications of tax policy. For instance, a good case can be made that graduated tax rates on gross casino revenue act as a deterrent to capital investment. When a company decides to commit additional capital to a casino property, it naturally expects to generate additional revenue to earn a reasonable return on its investment. However, if tax rates are graduated up, the casino company must consider the fact that any new injection of capital must generate substantially higher return than existing capital in order to cover the cost of the higher tax rate. The higher taxes will be reflected in the company's effective tax rate. While other market forces such as the quality of the operation, access to the property and demographics must be considered, the effective tax rate provides a good base comparison of state regulatory schemes.

Illinois Legislative Changes

In recent years, the Illinois legislature has enacted major changes to the riverboat gaming tax structure. In 1998, the flat 20% tax on adjusted gross receipts was abandoned in favor of a progressive scale ranging from 15% to 35% of gross revenue.[6] In 1999, the legislature eliminated the stayover admission fee along with the cruising requirement.[7] Illinois chose not to continue collecting stayover fees by eliminating phantom cruises similar to those conducted in Missouri, electing instead to assess only one $2 fee per patron rather than a $2 fee for each two hour "cruise".[8]

Impact of Continuous Boarding on Admission Fees

Although the Commission's rescission of the administrative rule restricting boarding was not implemented until several months into fiscal year 2000, continuous boarding had a significant impact on state and local admission fees. In total, state and local admission fees in FY 2000 were up 18.7% over FY 1999. This is due in large part to the fact that a customer's first stay-over gaming session

[5] For instance, Section 313.824, RSMo. requires that the riverboat gambling operators reimburse the Commission for the full cost of the staff necessary to protect the public. Last year this resulted in an average annual cost of $587,018 per gaming facility. However, these costs are not included in the revenue report issued by the Commission.

[6] Illinois P.A. 90-548, 1998. The scale imposes a tax of 15% on AGR up to $25 million; 20% between $25 and $50 million; 25% betwen $50 and $75 million; 30% between $75 and $100 million; and 35% over $100 million.

[7] SB 1017, Illinois General Assembly, 1999.

[8] Id.

comes sooner in a continuous boarding environment.[9]

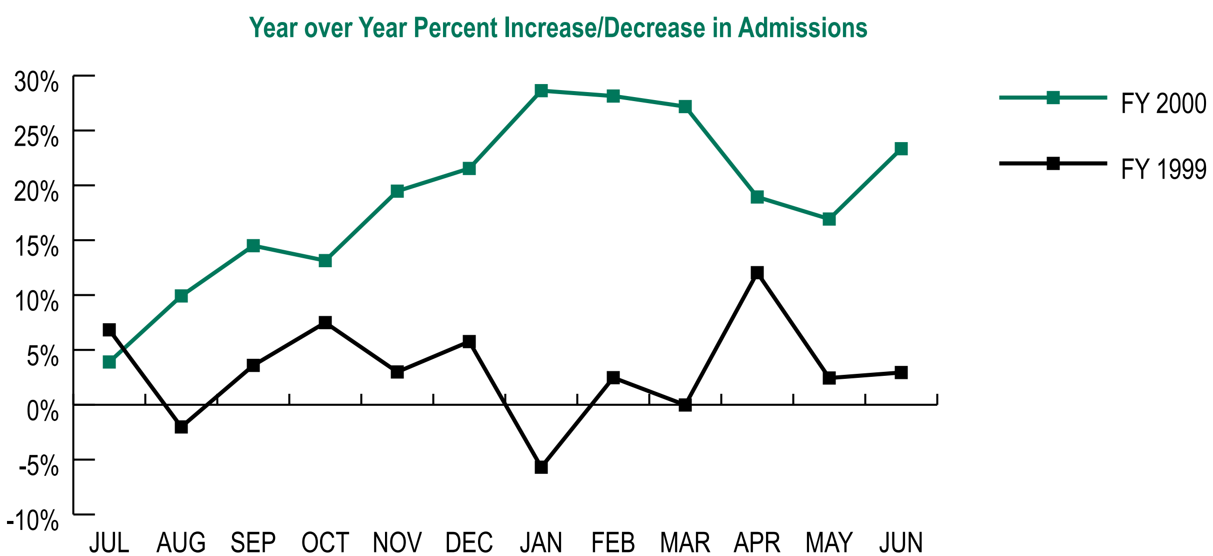
Comparing the Missouri Tax Rate to Other Jurisdictions

Until recently, Missouri's gaming tax was structured almost identically to Illinois, the state that hosts its principal competitors. The Missouri tax rate is significantly higher than the Iowa rate and is difficult to compare to casino operations at Indian reservations in Kansas because revenue figures are not available and no taxes are assessed. The Missouri tax structure was originally patterned after the Illinois system. However, recent legislative changes have been enacted in Illinois that now significantly distinguish its tax rates from Missouri's.

Furthermore, the addition of more Indian casinos in Kansas has increased competition in the Kansas City and St. Joseph markets. While the Kansas Indian casinos face a disadvantage because of their less convenient locations, the fact that they pay no state taxes and do not have loss limits provide them with a tremendous advantage over their Missouri competitors.[10] In addition, Indian tribes are attempting to secure permission to open casinos in Miami County, Kansas and at the Woodlands racing facility in Kansas. Both of these proposed sites have close proximity to casino operators in the Kansas City area and would have a substantial and immediate impact on jobs and state revenue.

[9] For a detailed discussion of the impact of continuous boarding, please refer to the section beginning on page 18 of this report.

[10] Indian casinos are not regulated by any independent agency. Therefore, Indian casino operators do not have to pay for the cost of regulation, which is significant.



Percentage Increase/Decrease in Admissions

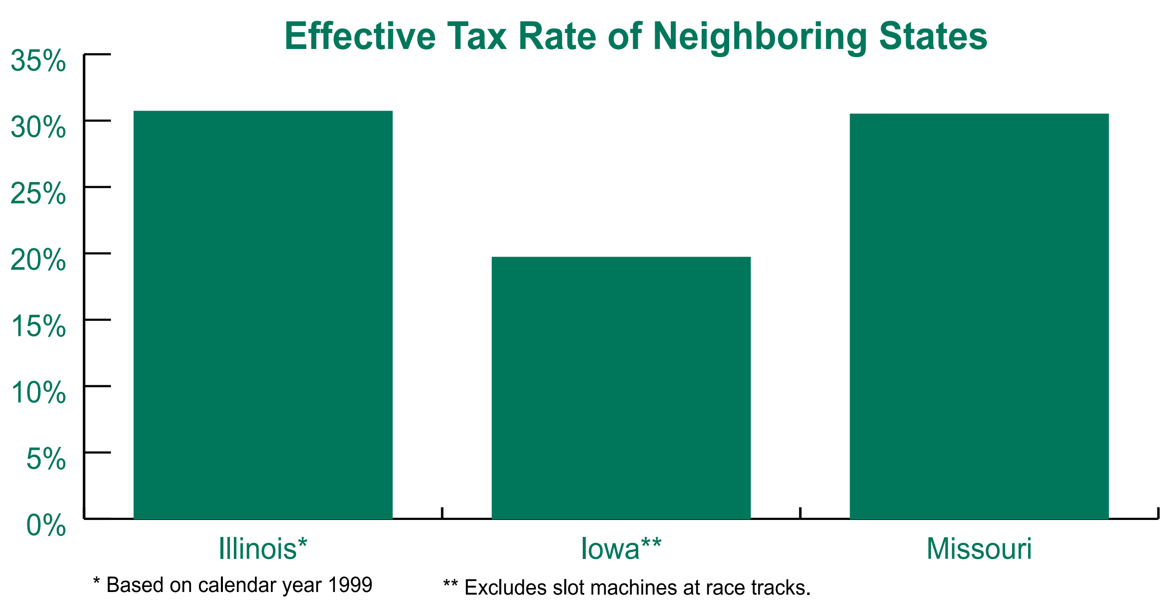
The Competitiveness of the Missouri Tax Rate

Last year the Commission opined that, as a result of the 1998 Illinois tax increase, Missouri's gaming tax rate on AGR is more conducive to capital investment than the Illinois' highly graduate tax system.[11] This theory seems to be borne out by the fact that the effective tax rate for Illinois operators remained virtually unchanged at 30.7% despite considerably lower admission fees. The $5.6 million reduction in admission fees was more than offset by an increase in the effective gaming tax rate from 26.0% to 27.5% due to the graduated tax rate rule. Overall, the strong AGR growth in Illinois resulted in the casinos paying gaming tax at the higher rate.

Illinois admission fees were lower last year because when the Illinois legislature authorized dockside gaming and permitted continuous boarding, it did not impose stay-over admission fees. Pursuant to state statute, Missouri operators are assessed a $2 admission fee for each patron attending each gambling excursion.[12] The Illinois law requires operators to pay only one $2 admission fee for each patron entering the casino.

[11] Missouri Gaming Commission Annual Report to the General Assembly, Fiscal Year 1999, pages 13-14.

[12] Because of the loss limit, the Commission continues to require operators to conduct 2-hour gambling excursions. Since Illinois has no loss limit, there are no "phantom cruises" in their new continuous boarding environment.



Furthermore, unlike Missouri, Illinois does not charge for the cost of Commission agents assigned to gaming facilities to protect the public. In FY 2000, Missouri casino operators were assessed $5,870,163.67 to pay for the cost of Commission agents assigned to gaming boats to protect the public.

There have been no changes to the Iowa tax rate since the first Missouri gaming facilities were licensed in 1994. Because its graduated rate tops out at 20%, Iowa has a lower tax on AGR than Missouri. In addition, Iowa's admission fee is set by the Commission and designed only to cover the cost of regulation and provide some local revenue. Therefore, Iowa gaming facilities pay an average of $1.40 less per admission than their Missouri competitors.

The Missouri tax rate is certainly one of the highest in the gaming industry. However, its structure has some inherent advantages over Illinois and the lower tax rate in Iowa does not appear to be affecting the competitiveness of the Missouri operators. Certainly, over the long term, the fact that Kansas Indian casinos pay no tax will have an impact on western Missouri operators. Finally, because Missouri has chosen the gradual approach to licensure by waiting to introduce new gaming capacity into a market until there is some indication that it can be absorbed, the tax rate has been effectively managed by the Missouri casino licensees.[13]

Effect of the Loss Limit on Competitiveness

Missouri operators continue to be at a competitive disadvantage when compared with gaming operators in neighboring states with no loss limits. The disadvantage continues despite expansion efforts and new property developments, which have produced facilities that are larger, provide superior comfort and more non-gaming amenities than their competitors in other states. For the sixth consecutive year, the data clearly shows that the loss limit reduces customer counts and gaming revenue. The inconvenience of the loss limit results in the export of Missouri gaming customers to other states and the loss of potential gaming revenue from local gamers and tourists.

This proposition is supported not only by the chart on page 13, but also by the fact that Illinois riverboats are capturing a larger market share than that state's population base represents. Missouri residents account for 76% of the St. Louis metropolitan area population base.[14] However, Missouri casinos in the St. Louis metropolitan area capture only 61% of the gaming revenue market.[15] This equates to an inequity of $97 million in relation to gaming revenue and $30 million in

[13] While many gaming operations struggled during the start-up period for riverboat gambling, all of the current licensees are generating positive EBITDA (Earnings Before Interest, Taxes and Depreciation).

[14] Rand McNally Metropolitan Statistical Areas, January 1, 1998 estimate.

[15] Based on Missouri fiscal year 2000 data from the Illinois Gaming Control Board and the Missouri Gaming Commission. The loss of revenue to Illinois continues to grow. Illinois casinos increased their share of the St. Louis market by 5% last year, netting them an additional $41.6 million in gaming revenue.

state and local taxes per year.

The Commission has spent thousands of hours working to improve enforcement of the loss limit. The Commission has and will continue to vigorously enforce the loss limit. In the past year, the Commission has fined casinos $660,000 for loss limit violations. Please note that the above findings are intended to satisfy the Commission's statutory mandate to report annually to the General Assembly on the effects of the loss limit on the competitiveness of the gaming industry in Missouri. The enactment of any changes in policy as a result of these findings are obviously the purview of the General Assembly and the Governor.

Casino Win Per Patron